# ILLHISER MAN'FG'.CO. VS. GALLEGO MILLS CO

## iew of the Recent Decision of the Supreme Court in This Case. Important to Banks Lending Money on Warehouse Receipts, and to Employes of Mining and Manufacturing Companies and persons Furnishing Supplies to Them.

## RRECTNESS OF COURT'S DECISION QUESTIONED

BY MR. JACKSON GUY.

itor of The Times-Dispatch:

Sir,—This case, decided by the Supreme Court of Appeals June 11, 1903,½ is one of interest by reason of its bearing upon the statute creating labor and supply liens, and the statute concerning warehouse receipts. This interest has probably been heightened with the public by the highly commendatory editorial notice of the case in the June number of the Virginia Law Register, in which the case is reported, and where it is characterized by the editor as being a case of "extreme importance," and by the publication in your paper by Mr. William L. Royall of several notices of the case, proclaiming the decision as one of the most important rendered in recent years, and as one worth millions of dollars to industrial enterprises.

Under these circumstances, I approach the task of submitting a review of the grounds upon which the court rests its decision, and of making some suggestions as to the correctness of that decision with misgivings, having been the commissioner of the court, whose decree confirming my report, was reversed. The appeal presented several controversies, but the leading one was a conflict between supply claimants and warehouse receipt claimants. And as to this the facts were these:

THE FACTS OF THE CASE.

The Gallego Mills Company, a corporation conducting a flour mill business, in order to increase its facilities for credit established within the mill what it styled its "warehouse," and upon the flour deposited there, whether ground or bought by it, filled out warehouse receipts and took them to bank and pledged them for loans. In this process it became indebted to the Union Bank of Richmond, and to the Savings Bank of Richmond in the aggregate sum of about $3,000. The appellants, who had furnished flour bags to the mills, claimed a lien therefor under the statute, and the question arose whether they, by virtue of the supply lien statute, were entitled to the proceeds of sale of the flour (amounting to about $2,900 as sold by the receiver of the court) or the banks, by virtue of the warehouse receipts pleged to them as above, the commissioner and the Chancery Court confirming his report, holding that Millhiser & Company were entitled to priority, while the Court of Appeals reverses that decision, and holds that the banks are entitled to the flour.

THE COURT'S MISTAKE.

The court places its decision upon the ground that the banks were purchases for value, without notice, and that it was not a conflict between lienors, but between a purchaser, on the one hand, and a lienor on the other.

It is in this particular that with great diffidence, I venture the opinion that the court has made a mistake. Their language (page 158) is:

"It will not be contended that the registry laws of the State have any application to a sale and delivery of personal property, and the question of 'priority' can only arise between claimants asserting a lien upon the property of their debtor.

"It is not a lien that the appellees are asserting upon the flour and wheat in question, but the legal title, the right of property made complete by possession and for value in due course of trade."

With entire respect for the court, I shall undertake to show that it was liens, and only liens, which the banks (the appellees) were asserting upon the flour.

On page 151 of the opinion, the court gives a copy of the warehouse receipt issued by the mills to the Union Bank, the same reading as follows:

"The Gallago Mills Company,
"Richmond, Va.
"No. 412. Warehouse Receipt.

"We have this day received in store for and on account of Union Bank, Richmond, Va., one hundred (100) (patent marked 21,339) barrels flour, to be held subject to the order of said bank, and to be delivered only on the surrender of this receipt.

"THE GALLEGO MILLS CO.,
"C. L. TODD, President.

"H. D. Riddick, Shipping Clerk Grain Receiver."

The court does not give a copy of the note, which pledged the warehouse receipt. A copy of the note given by the mills to the Savings Bank of Richmond is in the record, which was before the Court of Appeals, and is as follows (page 62 Sup. Rec.):

"$15,00. "Richmond, Va., Feb. 4, 1897.

"Fifteen days after date we promise to pay to ourselves or order, without offset, at the Savings Bank of Richmond, at Richmond, Va., for value received, having deposited as collateral security for the payment of this and any other liability to the holder thereof, the following property, with authority to sell, use, transfer or hypothecate said collaterals, or any that may be substituted thereof, or added thereto, for which purpose hereby constitute and appoint the cashier of the Savings Bank of Richmond true and lawful attorney:

"Warehouse receipt, No. 416, for one hundred (100) barrels flour mkd. "O," with the further right to call for additional security, in case there should be a decline in the market value thereof, and on failure to respond, said obligation shall be deemed to be due and payable without demand or notice, with full power and authority to the aforesaid attorney to sell, transfer, assign and deliver the above mentioned security, or any part thereof, or any substitute thereof, or any additions thereto, at public or private sale, at the option of the said holder or his assigns, on the non-performance of this promise, or the non-payment of any of the liabilities above referred to, at any time or times thereafter, without demand, advertisement or notice. The maker and endorser of this note hereby waives any benefit of exemption under homestead or bankrupt laws as to this debt.

"THE GALLEGO MILLS CO.,
"By C. L. Todd, Pt.

"THE GALLEGO MILLS CO.,
"By W. R. Todd, Act. Sec. & Treas."

(It should be explained that the note and warehouse receipt given by the mills to the Union Bank and those given by the mills to the Savings Bank are exactly alike, both being written on printed forms, where amounts and names were filled in to suit the case.)

The statement by the court, as above quoted, that it was a sale and not a lien that appellees were asserting, was, of course, a conclusion arrived at by them. The facts of the case simply were that the mills gave the banks warehouse receipts for the flour as collateral security for loans; and that the court construed the position occupied by the banks, as that of "purchasers," stating, with repetition, that the banks held the title to and possession of the flour.

I say, granted that the banks did have title to and a right to the possession of the flour, such a position did not essentially constitute them purchasers. They could not be purchasers by law when the contract made them pledgees. Modus et conventio vincunt legem.

Suppose possession of the flour had been delivered to the banks and (a) a conditional sale made of it or (b) a mortgage, or (c) a deed of trust; in each of these instances the banks would have had "the legal title and the possession," and yet their right would only have been a lien for the loan, over which the priority conferred by the supply-lien statute would clearly have prevailed. And it is difficult to see how the securing of its loan through means of a pledged, negotiable warehouse-receipt should have entitled the banks to an anvantage such as is given them by this decision.

As I look upon the negotiability of the receipt, the warehouse man or any one claiming by, through or under him, would be estopped to set up an equity or make any defense which would disturb an assignee of the banks in his claim upon the flour, but notice of its being a pledge.

With a clear conception as to this position of the banks, let us see what the Legislature has done. With it, a laborer and a man who furnishes supplies to a manufacturing company seem to have obtained as much, if not greater, favor than the holders of negotiable securities, for it says, Code 1887, section 2485, as amended, Acts 1891-'2, page 862:

THE STATUTE AND ITS HISTORY.

"All clerks, mechanics and laborers who furnish their services or labor to any mining or manufacturing company * * * shall have a prior lien on the franchises, gross earnings and on all the real and personal property of said company, * * * and no mortgage, deed of trust, sale, hypothecation or conveyance, executed since the 21st day of March, 1877" (the date of passage of the original act) "shall defeat or take precedence over said lien; and all persons furnishing supplies to a mining or manufacturing company, necessary to the operation of the same, shall have a prior lien upon the personal property of such company other than that forming part of its plant, * * * and also all the estate, real and personal, of such company, which said last lien, however, upon all such real and personal estate, shall be subject and inferior to any lien by deed of trust, mortgage, hypothecation, sale or conveyance, made or executed and duly admitted to record, prior to the date at which said supplies are furnished."

The history of this legislation is familiar. It is but a legislative echo of the judicial utterance that found its first imprint in Fosdick vs. Schall, when years ago, about the time of the passage of our statute, the Supreme Court of the United States proclaimed that a transportation company should, in case of its insolvency, first pay its employes and persons who furnished it with supplies necessary to its operation, what it owed to them before it paid anything to its mortgage creditors. Our Legislature, believing in the wisdom of this "equitable" rule of jurisprudence, took up the subject and enacted it into a "law," and extended the principle from transportation to mining and manufacturing companies. Whether the policy of the legislation was a mistaken one or not—and I judge our court must have considered it a mistake—it certainly had most respectable parentage, and, I submit, is founded in as much reason and public need as the liens and preferences given to mechanics, hotel keepers and others.

THE LANGUAGE OF THE STATUTE DISCUSSED.—HYPOTHECATIONS.

But, to return to the discussion: It is seen in the statute just quoted that laborers and supply-men are given a lien that is prior to liens created by mortgage, deed of trust, sale, hypothecation or conveyance. Now, while it is true that the legislative draughtsman did not put down in his category, eo nomine, every conceivable lien, and actually did omit to mention the lien of a party holding a pledge or collateral, yet I think it is but fair to infer from the comprehensive language used that, if not expressly embraced in the word hypothecation, it was intended that pledges and collateral should be covered by the other words used. Hypothecation, in the strict sense of the Roman law, is said to be a pledge without possession by the pledgee; but, to me in the connection used in the statute, it was intended to be understood in its popular sense where pledges of personal property and the giving of bonds and stocks as collateral security are commonly spoken of as hypothecations of them. The court, in its opinion (page 156), traces the origin of chapter 82 of the Code (section 1791 and seq.), concerning warehouse receipts, to the act of April 16th, 1874, the title of which it says is, "An act to prescribe how hypothecation of products and commodities shall be made, and to prohibit the hypothecation of consignments except on conditions." There, evidently, the word was used in a broad sense, embracing pledges and other such negotiations, and was intended to cover just such a thing as was done in this case, viz: the pledging of receipts with banks as collateral security for loans; and it is to be presumed that the Legislature in 1877, three years thereafter, when it created a preference in laborers and supply-men over liens by "hypothecation," had the hypothecation of warehouse receipts directly in mind.

THE LEGISLATURE OR THE COMMON LAW.

Assuming, then, that the Legislature, in the act quoted, intended to give a laborer or a supply man a preference, by virtue of his lien, over the lien which a man who held a pledge or a collateral had, does not this case present squarely this issue: Whether or not the Legislature had the power to say that Millhiser should have the flour as against the common law, which, as interpreted by our Court of Appeals, would say that the banks should have the flour because the warehouse receipts were, negotiable Can the Legislature amend the common law?

Many cases are cited by the court, but other than Lickbarrow vs. Mason, the case they rely upon most, seems to be Gibson vs. Stevens, 8 How. 384, where warehouse documents were taken and negotiated for advances made on the goods and then an attachement, in a suit on a claim against the original owners, was levied on the goods; the court sustaining the claim of the holders of the warehouse documents as against the attaching creditors. But is not that a long way from the case of a creditor who is given by statute a prior lien on those goods? The attaching creditor, unlike the supply lien creditor, had no priority, and it was a case in which plainly the maxim qui prior in tempore potior in jure should prevail.

ANOTHER DIFFICULTY WHICH THE COURT MEETS AND OVERCOMES.

But the court in order to make this decision had not only to declare that the holder of an hypothecated warehouse receipt, who had himself taken it from the warehouse man, to secure a loan which the holder had made upon it, was a purchaser for value and without notice, but it had to do more: The warehouse man (the Gallego Mills Company) was, as the court admits, not licensed as such, and had not complied with other requisites of the statute on warehouse receipts (Code 1887, chapter 82, sec. 1791 and seq.), so the court thereupon construes that this statute did not abrogate, but was only declaratory, of the common law; and reaches the conclusion that although there has been no pretensions to compliance with this statute, the warehouse receipts in this case are good at common law by which they are negotiable; that the statute having failed to repeal the common law, did not affect the negotiability which they possessed at common law.

A CURIOUS RESULT.

Now, howsoever this may be, and I hope I may be pardoned for doubting its correctness—for the very act of April 16, 1874, which the court says was the prototype of chapter 82, seems to be intended to be all-comprehensive, and expressly to have defined which warehouse receipts were to ne negotiable and which not—if the court is right there would seem to be a most curious result that would follow. Thus: Suppose there had been a compliance by the mills in every particular with the regulations of chapter 82. Then, the warehouse receipts in this case would have been negotiable by the statute; but by the terms of the statute the indorsee of the receipts is to be "deemed the owner of the property * * * so far as may be necessary to give effect to any sale to such person or to any pledge or lien for his benefit, created or secured by such transfer." In other words, he was to hold them for the purpose of fulfilling their hypothecation to him, and not for the purpose of giving effect to their sale to him; and, as already shown, the supply lien statute (section 2485) gives priority over a lien by hypothecation. Therefore, in that case clearly the banks would have lost. So that there follows this anomalous result: If one is the holder of a warehouse receipt, negotiable by statute, he loses to the supply man! If he holds one negotiable by comomn law, he prevails! This may be correct—and I hope no one will understand me as questioning in any particular the decisions of our highest court with other than the greatest deference—but if so what a confusion for the the laws of a State to be in! The court in its opinion cites authority (p. 156) to show that statutes are not presumed to alter the common law unless the act expressly so declares, and yet from the interpretation which the court gives to the common law, the statute and the common law certainly do not seem to agree with one another.

EQUITABLE ESTOPPEL, SAY THE COURT, IS THE TRUE DOCTRINE.

The court reaches and announces this conclusion, page 155:

"The doctrine upheld by the preceding authorities, that a warehouse receipt vests in a bona fide purchaser of it for value or in a bona fide pledge for value, the legal title to and possession of the property represented by the receipt, rests, not upon the theory of a symbolical delivery of the property, but upon the principles of equitable estoppel whereby one who has armed another with such indicia of title to the property that he may deceive innocent third parties and make them believe he is the real owner, will be estopped to set up any claim of title to the property as against one who is a bona fide purchaser of it without notice. This doctrine was enunciated in Wright vs. Campbell, 4 Barrows, 2046, and received pronounced judicial sanction in the early case of Lickbarrow vs. Mason, 2 Burn. and East., p. 63 (2 Smith's L. C., 9 ed., 1045, et seq.), repeatedly cited with approval, and never criticised, so far as we have been able to find, by text writers as well as in the decided case. See also McNeil vs. Bank, 46 N. Y., 325, where the doctrine is elucidated and a very instructive opinion delivered."

There can be no question as to the soundness of the doctrine that one who is a bona fide purchaser of the warehouse receipt, that is, a purchaser for value and without notice, gets a good and indisputable title to the goods. But, with respect, can any such condition of things be pretended in this case? The only parties to the transaction involved were the Gallego Mills Company on the one hand and the banks on the other, and the banks were certainly not parties "without notice" of the pledge. If they had transferred those receipts for value and without notice, to another, that other might have gotten a good and indisputable title, though I am not prepared to concede that to be clear as against the supply lien statute.

The cases cited by the court in the passage above quoted are ample to sustain the title of a party holding bills of lading without notice, but they go no farther. For the cases when read disclosed the fact that in every one of them it was the rights of a third party into whose hands the bill of lading had passed from the party to whom they were originally issued that the courts sustained, as against persons claiming under the consignor.

The opening sentence of the annotator, 2 Sm. L. C. (9th ed.), p. 1089, upon the case of Lickbarrow vs. Mason, brings out, I think, most clearly the point in question. He says:

"This celebrated case involves two important propositions. The former is, that the unpaid vendor may, in case of the vendee's insolvency, stop the goods sold in transitu. The latter, that the right to stop in transitu may be defeated by negotiating the bill of lading with a bona fide indorsee."

The last of the cases cited by the court in the passage quoted is McNeil vs. the Bank, and to shew that it will not support the court in its decision in this case, I think it is only necessary to copy the opening sentence of the syllabus, viz.:

"When the owner of property confers upon another an apparent title to, or power of disposition over it, he is estopped from asserting his title as against an innocent third party, who has dealt with th eapparent owner in reference thereto, without knowledge of the claim of the true owner. The rights of such third party, do not depend upon the actual title or authority of the one with whom he dealt, but upon the act of the owner, which precludes him from disputing the title or authority, he has apparently conferred."

In other words, these cases are but in conformity with the well known principle of mercantile law that a payee or endorser may confer a better title upon his transferree than he himself has.

FIDELITY INSURANCE COMPANY VS. ROANOKE IRON WORKS.

It should be stated that the court also bases its conclusion upon this case, reported in 81 Fed. 439; upon that portion of Judge Simonton's opinion which disposes of the claim of Crocker Brothers. I submit that the court was unfortunate in selecting this case as a basis for its decision. It is a full and exhaustive opinion of Judge Simonton's, and it is hard to give an analysis of it in a short space.

As to the Crocker Brothers' claim:

"The Roanoke Iron Company was the manufacturing company in that case, and against it parties were asserting liens for supplies under the statute (V. C., sec. 2485), and the question was, whether the iron in the possession of Crocker Brothers was a part of the personal property of the Roanoke Iron Company at the date when the supplies were furnished? Judge Simonton concluded that it was not, and the court has followed him in the argument by which he reached that conclusion instead of, as I humbly submit would have been right, following him in what is said with reference to the claim of the Philadedphia Warehouse Company. It seems that the Roanoke Iron Company consigned to Crocker Brothers the iron in question, issuing a bill of lading therefor; that Crocker Brothers received the iron and placed it upon a lot of their own in the city of Roanoke; they made advancement upon this iron pursuant to their agreement to do so as set out in their letter to the company; they being thereby constituted the sole and exclusive agents of the company for the sale of the iron and agreeing to advance on it as received, to the extent of three-fourths of its value. The delivery of the very iron had been made to them and under that contract they had advanced on it. The reasoning of Judge Simonton in respect to this is set out in the court's opinion. Now, whatsoever may be said as to its correctness or incorrectness, I venture no comment upon it, because, whether right or wrong, it is not the case we are dealing with. If there is a resemblance in it to the contract between the banks and the mills in this case, resemblance becomes identity when a comparison is made between the cases of the Philadelphia Warehouse Company's claim and that of the banks inthe case I am discussing.

As to the Philadelphia Warehouse Company's claim:

The Philadelphia Warehouse Company rented some land from the Roanoke Iron Company and styled the same its yards. The latter delivered to the former on these yards hundreds of tons of iron, and on the iron so delivered made loans amounting to thousands of dollars; all the output of the furnaces were delivered on these yards, and from the iron bulked there, shipments were daily made by the Roanoke Iron Company to its customers, precaution being taken that the depletion from the stock should not encroach upon the sufficiency of the security of the Warehouse Company. This arrangement between them was effected by what was called an invoice consignment contract, in which, after the delivery of the iron and the advance of the money as stated, it was stipulated that the Warehouse Company for this advancement was to have a lien prior to all other claims upon this merchandise, and in case the money was not paid the Warehouse Company was to have the right to sell the iron and apply the proceeds to the payment of its debt.

Judge Simonton then says that the first question which arises is, whether the arrangement between the iron company and the warehouse company is a valid pledge. And in this connection states, page 445: "Two things are essential to constitute a pledge :First, possession by the pledgee; second, that the property pledged be under the power and control of the creditor. 'The difference,' says Bradley, J., in Casey vs. Cavaroc, 96 U. S., 477, 'between a mortgage and a pledge is that title is transferred by the former, and possession by the latter.'" He proceeds:

"The next question is, Is this lien of the pledgee prior to that of the supply creditors? As has been seen, the warehouse company holds the iron in pledge. The distinctive character of the pledge is that it does not transfer title, but transfers possession. Bradley, J., in Casey vs. Cavaroc, supra. It is a bailment of personal property, as security for some deed or engagement. Story, Bailm, section 286. The general property remains in the pledgor, with a qualified property in the pledgee, giving the pledgee every right which can secure the possession. It is, in the strictest sense, a common law lien. Peck vs. Jenness, 7 How., 620. The supply creditor claims under the statute law of Virginia. The law now of force in Virginia is the act approved February 15th, 1892 (Acts 1891-'92, page 362, chapter 224, amending the Code of Virginia adopted in 1887). This Code of Virginia is a statute speaking from its date, and has all the formalities of an act." The judge concludes in the following lucid and emphatic language, page 447:

"This iron held by the warehouse company was the property of the iron company not used in its plant, a bailment in the hands of the warehouse company, upon which it had a lien. The act of the Legislature of Virginia, of force when the contract was made, and held to be valid in Virginia Development Co. vs. Crozer Iron Co., 90 Va., 126; 17 S. E., 806, declares that the claims of persons furnishing supplies have a prior lien on all the personal property of a corporation not a part of its plant. This act entered into and was a part of the contract made by the warehouse company, and it received the bailment subject to the provisions of the act. This case seems to come within the words of the statute, and the conclusion cannot be avoided that the supply creditors have a lien on this iron prior to that of the warehouse company."

Now, I submit to the judgment of an impartial profession and public that if this case is to be looked to as an authority in the case at bar, then the only question left for solution is, whether the arrangement between the Gallego Mills Company and the banks was a pledge of the flour. If it was a pledge, Fidelity Insurance Company vs. Roanoke Iron Company says the supply liens come first. That it was a pledge, the terms of the note given for the money as set out in this paper, unmistakably show.

The following authorities are relied on to sustain the position taken in this paper: that the banks held merely a lien; that they were, nor indorsee; that it is only bona fide indorsees from pledgees that are entitled to the position of a purchaser for value and without notice, and that the doctrine of estoppel enunciated by the court has no application to the case: 2 Jones on Liens, sections 2, 3; Story on Bailment, sections 287, 312; Jones on Pledges, section 7; 2 Bart. Chy. Pr., section 317; Gilliatt vs. Lynch, 2 Leigh, 493. This case I look upon as one of great value in defining the rights of the holders of negotiable paper held as collateral security. I quote as follows from page 502 of the opinion of Green, J., concurred in by the other judges:

"The deposit of Lynch's notes indorsed in blank, as a collateral security for a debt not equal to their amount, did not give to Gilliatt and Hughes and Armistead and absolute property in them on account of their negotiable character. On the contrary, they were bound by their contract, jointly, to return the notes, precisely in the form in which they received them, without a retransfer of them by indorsement, if Perkins paid his debt. * * * * For as to the immediate parties to a negotiable note, and as between an immediate indorser and indorsee, such a note has no peculiar character whatever distinguishing it from any other contracts, however evidenced. It is open to all objections to, the consideration, or want of consideration, and all set-offs and equities between those parties, which would be available in all other contracts not founded on a deed. It is only where a third party acquired an interest by indorsement for full value that it acquires as to him the character of a negotiable security, entitled to the benefit of the law merchant against all other parties, except his immediate indorser."

I need only to add that all persons are presumed to make their contracts subject to the law then in force; and hence, that if these banks took warehouse receipts from a manufacturing company, such as was the mills in this case, they did so with eyes open to the contingency that a laborer or a supply-man might turn up with a lien, upon which the statute conferred a preference over them. This principle, recognized by Simonton, J., supra, was also recognized by the Supreme Court of Appeals of Virginia, in Virginia Development Company vs. Crozer, 90 Va., 126, where the court then held that a supply lien overrode a deed of trust recorded a year before. Such being the case, the banks in this case could not be holders for value without notice.

THE REGISTRY LAWS.

And, that while it is true that the registry laws of the State have no application to a sale and delivery of personal property, as asserted in the opinion of the court (see paragraph first copied herein), it is true that they do apply to and include all liens upon, or conditional sales of, or reservations of use in goods and chattels. (See chapter 108 of the Code, secton 2461 and seq.).

EVERYBODY THE KEEPER OF A WAREHOUSE, AND AN ABUNDANT CROP OF SECRET LIENS.

And, that if the Gallego Mills Company could, without making a pretense of complying with the requirements of the statute concerning the keeping of a public warehouse, which the court in its opinion admits was the case (p. 150 "as it is not pretended that * * * the warehouse is conducted as a licensed warehouse under the statute"); and without making a pretense of taking and keeping the goods of others on storage, which the court in its opinion likewise admits, (p. 151, "the fact that the Gallego Mills Company did not happen to store in its warehouse the goods of other merchants and manufacturers, but stored alone, as seemed to have been the case, the products of the business conducted by it as a milling concern * * *, is, as we think wholly immaterial"), pledge its own goods, the possession of which remained with itself, undisturbed in its own mill, by passing to a bank a receipt or certificate for those goods, it is not perceived why any manufacturer or merchant in the city, wholesale or retail, may not do the same thing, and in that way undoubtedly violate the intent as well as the letter of the registry laws by creating an abundant crop of secret liens.

In conclusion, it might be regarded as the peculiar province of an impartial public to comment upon a court's decision; certain it is that its merits must rest with such a tribunal. If that is the proper ethical view to take of the matter, and admitting my former connection with the case as already stated, my apology must be that I am following the pace set by Mr. Royall and the editor of the Virginia Law Register, both of whom have expressed public approbation of the opinion as already stated, although both had filed briefs in the argument of the case before the Court of Appeals.

Richmond, Va., Sept. 23, 1903.

All That is Good.

Orthodox religious beliefs and practices continue to find their strongest support in the South. The Alabama Legislature has just enacted a law prohibiting Sunday base-ball games, tennis, golf and foot-ball, and making violation a misdemeanor.—Springfield, Mass., Republican.